BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 1999-007-G - ORDER NO. 1999-712

OCTOBER 7, 1999

IN RE:	Annual Review of the Purchased Gas Adjustments (PGA) and Gas Purchasing Policies of South Carolina Pipeline Corporation.	) ORDER ON PRUDENCE, √ MR) PGA, AND RELATED) MATTERS)

This matter comes before the Public Service Commission of South Carolina (the Commission) on its annual review of the Purchased Gas Adjustments (PGA) and Gas Purchasing Policies of South Carolina Pipeline Corporation (SCPC).

I. INTRODUCTION

Commission Order No. 87-1122 provides that an annual review be conducted of SCPC's PGA and Gas Purchasing Policies. In this proceeding, the review period is January 1998 through December 1998. Petitions to Intervene were filed by the Consumer Advocate for the State of South Carolina (the Consumer Advocate), Chester, Lancaster, and York Natural Gas Authorities (the Authorities), the City of Orangeburg (the City), the South Carolina Energy Users Committee (SCEUC), South Carolina Electric & Gas Company (SCE&G), and Nucor Steel (Nucor).

A hearing was held in this matter on August 4, 1999, at 10:30 a.m. in the offices of the Commission, with the Honorable Philip T. Bradley, Chairman, presiding. SCPC was represented by Catherine D. Taylor, Esquire, and Mitchell Willoughby, Esquire. SCPC presented the testimony of Asbury H. Gibbes, Paul V. Fant, Patricia B. Jackson, Cynthia A. Kase, John S. Beier, and Dr. Julius A. Wright. The Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire, and presented the testimony of Richard Hornby. The Authorities were represented by James W. Sheedy, Esquire; SCEUC was represented by Daniel B. Lott, Jr., Esquire; SCE&G was represented by Patricia T. Smith, Esquire; and Nucor was represented by Russell B. Shetterly, Jr., Esquire. The City did not appear at the hearing. The Commission Staff (the Staff) was represented by F. David Butler, General Counsel. The Staff presented the testimony of Norbert M. Thomas and Brent L. Sires.

Prior to the hearing, SCPC filed a motion to strike a substantial portion of Consumer Advocate witness Hornby's testimony on res judicata grounds. SCPC argued that the issues and claims concerning firm capacity acquired by SCPC from Transcontinental Gas Pipe Line (Transco) beginning in November 1997 (Sunbelt capacity) were litigated by the Consumer Advocate and decided adversely to the Consumer Advocate by Commission Order No. 97-477 in Docket No. 97-009-G. In response, the Consumer Advocate contended that the issues addressed in Mr. Hornby's testimony in this case are not identical to those raised and ruled on by the Commission in Docket No. 97-009-G. The Consumer Advocate further contended that in Docket No. 97-009-G Mr. Hornby urged the Commission not to approve the contract for the Sunbelt capacity with Transco on the grounds that it was not necessary to ensure reliable service to firm customers, while his testimony in this proceeding focuses on the reasonableness of SCPC's utilization of its capacity and the implication of that utilization on the reasonableness of its rates. We held SCPC's motion to strike in abeyance and stated that the motion would be addressed in the final order in this matter.

II. FINDINGS OF FACT AND CONCLUSIONS OF LAW

A. GAS PURCHASING POLICIES AND PRACTICES

As an initial matter, we find that SCPC's purchasing policies and practices were prudent during the review period. SCPC witness Fant testified in detail about SCPC's recent gas purchasing policies and practices, concluding they were prudent. [Tr. p. 48, line 18 - p. 50, line 16; p. 54, lines 10-12; p. 55, line 11 - p. 57, line 18]. SCPC witness Gibbes reached the same conclusion, as did Staff witness Sires. [Tr. p. 16, lines 3-8; p. 18, lines 18-22; p. 241, lines 16-22]. No evidence to the contrary was presented at the hearing.

During the review period, SCPC maintained a reliable and flexible portfolio of gas supply, storage, and capacity. [Tr. p. 48, lines 20-21]. SCPC continued to demonstrate that it places a high level of importance on securing reliable gas supplies and on making prudent decisions in purchasing its gas supplies. [Tr. p. 230, lines 24-27]. No supply problems were noted on the company's system during the review period. [Tr. p. 230, line 27 - p. 231, line 1; p. 241, line 23 - p. 242, line 1]. In addition, SCPC continues to exhibit its capabilities to secure gas supplies in a prudent manner and at reasonable costs. [Tr. p. 231, lines 2-12; p. 242, lines 2-5]. We therefore find that SCPC's gas purchasing policies and practices were prudent during the period of January 1998 through December 1998.

B. ADHERENCE TO TARIFF

We also find that during the review period SCPC properly adhered to the tariff provisions relating to recovery of its gas costs. There was no dispute as to whether gas costs were properly recovered during 1998. SCPC witness Jackson described the procedure the company followed for gas cost recovery, concluding that calculations were made in compliance with the approved tariff and Commission directives. [Tr. p. 71, line 4 - p. 72, line 5; p. 75, line 16 - p. 77, line 16]. Staff witness Thomas presented the Commission Staff's audit of the company's cost of gas, verifying that the cost of gas for the review period was properly accounted for. [Tr. p. 214, line 15 - p. 220, line 14; p. 222, line 2 - p. 223, line 6; p. 223, line 24 - p. 224, line 20]. Accordingly, we find that for the period of January 1998 through December 1998 SCPC's gas costs were accurately stated, SCPC's gas cost recovery was calculated in compliance with Commission orders and the approved gas tariff, and the monthly cost of gas rates resulted in the precise recovery of actual gas costs incurred by the company.

C. INDUSTRIAL SALES PROGRAM-RIDER

Next, we find that the Industrial Sales Program Rider (ISP-R) continued to produce benefits for SCPC's firm customers and that the program should be continued. As SCPC witness Fant testified, the ISP-R allows SCPC to assign delivered gas costs to industrial customers at prices that are competitive with alternative fuel prices and enables SCPC to make interruptible sales that otherwise might not be made. [Tr. p. 52, line 12 - p. 53 - line 6]. Staff witness Sires confirmed that the ISP-R is needed for SCPC to effectively compete with alternate fuels in the industrial market. [Tr. p. 233, line 15 - p. 236, line 4; p. 252, lines 16-20]. The ISP-R also gives SCPC the flexibility to curtail interruptible customers to satisfy firm customer demands when necessary. [Tr. p. 53, lines 7-8]. The ISP-R promotes more efficient use of SCPC's facilities, helps to recover a portion of SCPC's fixed costs through industrial sales, allows SCPC to exert purchasing power in interruptible gas markets so that natural gas is obtained at better terms and prices, and provides additional flexibility and reliability to SCPC's system. [Tr. p. 53, line 8 - p. 54, line 8]. For these reasons, the ISP-R should be continued without modification.

D. 20,000 DEKATHERMS PER DAY REQUIREMENT

By Commission order, SCPC is required to assign to the weighted average cost of gas (WACOG) 20,000 dekatherms of the least expensive daily delivered gas volume entering SCPC's system. [Tr. p. 71, lines 15-16; p. 76, lines 9-11; p. 232, line 22 - p. 233, line 1; p. 238, lines 11-19]. During the period under review, this requirement caused SCPC to lose approximately $2.1 million in approved margins and caused its sale-for-resale customers to lose approximately $223,000. [Tr. p. 72, lines 6-13; p. 76, lines 17-21]. Customers whose gas purchases were made at the WACOG realized reductions in gas cost of approximately $2.5 million as a result of this requirement. [Tr. p. 232, lines 11-16; p. 239, lines 5-10].

In this proceeding, no evidence was presented that would warrant modifying the 20,000 dekatherms per day requirement. Rather, Staff witness Sires testified that this level of lowest cost gas entering the WACOG was acceptable and that the Commission Staff recommended that it be continued. [Tr. p. 232, line 18 - p. 233, line 14; p. 238, line 19 - p. 239, line 4; p. 243, line 24 - p. 244, line 21]. No other witness or party took exception to Staff's recommendation. Accordingly, SCPC should continue to assign 20,000 dekatherms of the least expensive daily delivered gas volume to the WACOG.

E. PILOT HEDGING PROGRAM

We also find that SCPC's pilot hedging program provides benefits to firm customers and should be continued. The primary objective of the program is to reduce price volatility through the purchase of gas at the average market price over the long term. [Tr. p. 96, line 13 - p. 97, line 8; p. 111, lines 5-7; p. 122, lines 6-10]. The Commission approved the pilot hedging program in 1995, initially allowing SCPC to hedge up to 30% of purchases for firm customers. The Commission allowed subsequent increases in volumes that may be hedged. Since 1997, SCPC has been allowed to hedge 75% of estimated purchases for firm customers. [Tr. p. 111, lines 4-15; p. 122, lines 4-16].

After the extreme natural gas price volatility during the winters of 1996 and 1997, SCPC implemented the Kase HedgeModel$_{TM}$ in February 1998. The Kase HedgeModel$_{TM}$ is a refinement of the program SCPC had in place. It provides for greater reductions in volatility through a more strategic, statistically based, and longer term hedging model. The Kase HedgeModel$_{TM}$ attempts to stabilize SCPC's price of gas by locking in purchases of futures at statistically low prices, protects SCPC's customers from extremely high prices by requiring the purchase of call options when the market threatens a run to higher prices, and reduces the probabilities that SCPC's customers will have to pay extreme prices for natural gas. [Tr. p. 112, line 5 - p. 113, line 4; p. 122, line 17 - p. 123, line 5].

We find that SCPC's hedging program continues to achieve its primary objective of reducing price volatility and that the current maximum level of 75% of firm purchases is appropriate for achieving that objective. These findings are supported by the testimony of SCPC witness Beier and Staff witness Sires. [Tr. p. 116, line 4 - p. 118, line 2; p. 125, lines 2-19; p. 132, lines 7-18; p. 134, lines 1-24; p. 231, line 26 - p. 232, line 10; p. 258, line 15 - p. 261, line 3]. In addition, the program satisfies the criteria, identified by SCPC witness Kase, for a prudent hedging program. [Tr. p. 100, line 18 - p. 101, line 4; p. 103, line 3 - p. 104, line 19]. Continuation of the pilot hedging program is therefore approved at the current allowed volumes of 75% of estimated gas purchases for firm customers. We reserve the right to modify the program in the future, should present facts or circumstances change.

F. CONSUMER ADVOCATE'S PROPOSED TARIFF CHANGE

Finally, we find that the issue raised by Consumer Advocate witness Hornby's proposed tariff change has been litigated by the Consumer Advocate and decided in a previous Commission order and that, in any event, the proposal should be denied on the merits. Witness Hornby proposed that SCPC be required to augment capacity release revenues credited to the WACOG each month by the difference between the monthly demand charges for the incremental Transco capacity (Sunbelt capacity) and the capacity release revenues for the month. [Tr. p. 151, lines 2-6; p. 202, line 5 - p. 203, line 2]. He justified this proposal upon two facts presented in his testimony: (1) that SCPC does not need to hold the Sunbelt capacity to provide reliable service to firm customers at reasonable rates and (2) that firm customers are not receiving a net benefit from the Sunbelt capacity. [Tr. p. 151, lines 8-11].

The Consumer Advocate is attempting to relitigate in this docket the same issues that were decided in Docket No. 97-009-G. Order No. 97-477 in Docket No. 97-009-G rejected the same two bases for Mr. Hornby's recommendation in this case, concluding: We have examined this acquisition and believe that the record clearly demonstrates the need for and benefits associated with this [Sunbelt] capacity, in addition to the capacity that SCPC currently holds. The order discussed six specific reasons for denying Mr. Hornby's claims, found that acquisition of the Sunbelt capacity was reasonable and prudent under the circumstances, and approved both the acquisition of the capacity and SCPC's recovery of the charges associated with this capacity.

Although we deny SCPC's Motion to Strike Hornby's testimony, in the interest of hearing the positions of all parties, we do not believe Hornby's testimony is meritorious.

First, as previously stated, the proposal is based upon the assertion that there is no need for SCPC to hold the Sunbelt capacity. This assertion is incorrect, as is Mr. Hornby's conclusion that the Sunbelt capacity constitutes excess capacity. The Commission rejected the identical contentions in Order No. 97-477, in which the acquisition of the Sunbelt capacity was found to be prudent and necessary. [Tr. p. 21, line 13 - p. 22, line 4; p. 27, lines 12-21].

Moreover, Mr. Hornby's calculation of SCPC's capacity improperly equated the limited capability of the liquefied natural gas (LNG) storage facilities at Bushy Park and Salley with the firm transportation (FT) capacity SCPC holds on the interstate pipelines. In Order No. 97-477, the Commission held that, in computing SCPC's reserve, the limited capability available from the LNG facilities should not be equated with the FT capacity on the interstate pipelines. [Tr. p. 22, lines 5-21; p. 27, line 22 - p. 28, line 7].

Currently, SCPC customers hold firm contract demand of 305,051 dts/day, which the company is obligated to serve 365 days a year. SCPC has a total of 300,624 dts/day of firm capacity on the interstate pipeline systems, including the Sunbelt capacity. Thus, the total interstate delivery capacity available to SCPC 365 days a year is 4,427 dts/day less than current obligations. [Tr. p. 23, lines 3-9].

The two LNG facilities have a combined send-out capability of 153,150 dts/day when completely full; natural boil-off reduces this amount daily, regardless of use. The LNG capability is severely time limited, however, consisting of 91,890 dts/day for 10 days at Salley and 61,260 dts/day for 16 days at Bushy Park. Assuming there are no upstream supply or pipeline interruptions and both LNG facilities were able to support the system at full capacity, SCPC has approximately 49% capacity over its FT obligations for 10 days, only an approximately 19% reserve for the next 6 days, and a negative reserve thereafter. [Tr. p. 23, line 10 - p. 24, line 4; p. 28, lines 8-24; p. 289, line 19 - p.

290, line 17]. Considering the limitations associated with the LNG capability, anticipated growth on SCPC's system, and the advantages presented by having additional capacity from Transco, [Tr. p. 24, line 5 - p. 26, line 6; p. 29, lines 1-7], we find that the Sunbelt capacity is needed to serve firm demand reliably and therefore benefits SCPC's firm customers.

We disagree with Mr. Hornby's claim that the demand for firm natural gas capacity is not growing in South Carolina. As shown in Mr. Hornby's own Exhibit No. 9 (RH-3), total firm customer sales grew from 30,347,000 dts in 1993 to 38,505,000 dts in 1997, for an average growth rate of almost 5% per year. [Tr. p. 287, line 9 - p. 288, line 4; p. 295, line 18 - p. 296, line 4; p. 298, line 24 - p. 299, line 11]. Mr. Hornby's focus on 1998 alone does not accurately indicate firm growth trends. As explained by SCPC witness Wright, firm gas sales declined during 1998 due to an abnormally mild winter. That year had only 2,141 heating degree days while a normal year in South Carolina has approximately 2,582 heating degree days. [Tr. p. 288, lines 5-15; p. 299, line 18 - p. 300, line 4].

In addition, Mr. Hornby's analysis of SCPC firm sales excluded a substantial volume of sales that SCPC treats as firm load for planning purposes. Mr. Hornby included only firm sale-for-resale and firm industrial sales. However, SCPC makes additional sales to firm sale-for-resale customers which are used to supply their industrial ISP-R customers. Since these sale-for-resale customers pay the full firm demand charge, SCPC treats these volumes as firm load for planning purposes. When these sales are added to Mr. Hornby's analysis, SCPC's total planning firm sales are growing at an average rate of 4.4% per year. [Tr. p. 289, lines 7-18].

Other factors also indicate growth of firm demand on SCPC's system. South Carolina is one of the faster growing states in the nation and has ranked among the top in terms of new factories and new employment growth. [Tr. p. 288, line 19 - p. 289, line 6; p. 296, lines 4-8]. In addition to the increased economic development in areas served by SCPC's system, growth in firm demand can also be expected due to age and reliability problems with the sale-for-resale customers' propane air facilities. In Order No. 97-477, the Commission stated that these factors were likely to cause increased demand requirements on SCPC's system. [Tr. p. 25, lines 4-15].

For all the above reasons, we reaffirm the findings in Order No. 97-477 that acquisition of the Sunbelt capacity was prudent, reasonable, and necessary for SCPC to reliably serve its firm customers. We also reaffirm the findings that the Sunbelt capacity benefits firm customers.

Mr. Hornby testified that the Sunbelt capacity benefited SCPC shareholders by allowing them to earn \$3.9 million in incremental margins from interruptible sales and transportation. He reached this conclusion based upon the fact that the margins he calculated for interruptible sales and transportation for 1998 were \$3.9 million higher than those margins for 1996. Thus, he concluded, these additional margins must be attributable to SCPC's acquisition of the Sunbelt capacity. [Tr. p. 149, line 15 - p. 150, line 18]. We reject Mr. Hornby's analysis for the reasons discussed by SCPC witness Wright.

As Dr. Wright pointed out, using Mr. Hornby's own calculations, SCPC's interruptible margins in 1993 were more than $400,000 greater than the margins in 1998. This demonstrates that any increase in interruptible margins are not attributable to the acquisition of the Sunbelt capacity. [Tr. p. 290, line 18 - p. 292, line 20; p. 296, line 19 - p. 297, line 8; p. 300, lines 11-20; p. 304, line 7 - p. 305, line 4]. Moreover, Mr. Hornby's assertion that acquisition of the Sunbelt capacity allowed SCPC to earn additional margins by eliminating winter curtailments, [Tr. p. 159, lines 1-18], is not supported by the evidence. His reliance upon a statement contained in the 1998 10K filing of SCANA is misplaced. The 10K filing indicated that increased gas transmission sales margins and volumes and fewer curtailments were attributable to a $50 million internal pipeline expansion, not to Transco's Sunbelt project. [Tr. p. 305, line 13 - p. 306, line 5].

Mr. Hornby's analysis shows only that SCPC's margins from interruptible sales have fluctuated from year to year. [Tr. p. 292, lines 13-20; p. 305, lines 4-13]. In fact, Mr. Hornby conceded that a number of factors other than additional upstream capacity would have influenced the changes in interruptible margins. [Tr. p. 196, line 7 - p. 197, line 19]. He also admitted he could not calculate the impact of the additional capacity on SCPC's margins, but had intuitively concluded that there was a relationship between the additional capacity and SCPC industrial margins. [Tr. p. 207, lines 7-24]. Because his underlying assumptions are not supported by the evidence, we disagree with Mr. Hornby's suggestion that acquisition of the Sunbelt capacity has benefited SCPC's shareholders to the exclusion of its firm customers.

Based upon the foregoing, we deny the Consumer Advocate's request to require that SCPC credit to the WACOG each month the difference between the monthly demand charges for the Sunbelt capacity and the capacity release revenues for the month.

G. PROPOSAL OF THE COMMISSION STAFF

Finally, we will consider the testimony of Staff witness Sires, wherein he recommended that all upstream demand charges incurred by SCPC be evenly allocated to firm customers based on their contract MDQ volumes. Additionally, the Staff recommends that capacity release credits that are now credited to the Form 1 cost of gas calculation be credited to the DMI cost of gas calculation. [Tr. page 236, lines 8-11]. We have considered these proposals, and believe that they may have some merit, in that they attempt to address collection of demand costs from all firm customers. However, we believe that further investigation is necessary before we consider implementing the Staff's proposals as a final policy, or any alternative proposals that would address collection of demand costs from all firm customers. We therefore deny the proposals at this time. However, we would request that Staff further investigate the proposals, and after consultation with the Company and other parties as necessary, report back, if appropriate, to this Commission at a later time.

IT IS THEREFORE ORDERED THAT:

1. SCPC's gas purchasing policies and practices during the period January 1998 through December 1998 are found to be prudent.

2. SCPC is found to have properly adhered to the gas cost recovery provisions of its gas tariff during the period January 1998 through December 1998.

3. The requirement that SCPC assign to the WACOG 20,000 dekatherms of the least expensive daily delivered gas volume shall be continued.

4. The ISP-R shall be continued without modification.

5. The pilot hedging program shall be continued at 75% of estimated gas purchases for firm customers.

6. The Consumer Advocate's proposed tariff change is hereby denied.

7. The Commission's Staff proposals related to the allocation of upstream demand charges incurred by SCPC are denied. However, Staff is directed to further investigate this issue, and, if appropriate, report back to the Commission at a later time.

8. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Philip T. Bradley
Chairman

ATTEST:

Gary E. Walsh
Executive Director

(SEAL)